New Mandatory Disclosure Rules: Reportable Transactions & Uncertain Tax Treatments

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Mandatory Disclosure Rules

- Background & Current Rules
- *BEPS Action 12* & Federal Budget 2021 Proposals
- Amended "Avoidance Transactions"
- Amended "Reportable Transactions"
- Proposed New "Notifiable Transactions"
- Proposed New "Uncertain Tax Treatments"

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Background

Mandatory Disclosure Rules

- Lack of timely/relevant info on aggressive tax planning strategies is one of main reported challenges to tax authorities worldwide

- Mandatory disclosure rules allow tax authorities to react quicker to risk of tax avoidance

- *Income Tax Act (Canada)* contains rules requiring certain transactions to be reported to the CRA to target specific tax risk areas

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OECD – BEPS Action 12

- Organization for Economic Co-operation & Development ("OECD")
  - International body with recommendations relating to enactment of mandatory disclosure rules

- *Base Erosion and Profit Shifting ("BEPS"), Action 12*
  - Many such measures have already been implemented in a number of countries with comparable tax systems
  - U.S. & Australia – reporting tax uncertainty in audited F/S

- CRA has stated the existing Cdn tax legislation is not sufficiently robust to address these concerns.

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Background – Current Rules

2010 Federal Budget

- Introduced March 2010, enacted June 2013, but applies retroactive to 2011
- Section 237.3 – intended to curtail tax evasion/avoidance
- "Reportable Transaction" – if it constitutes
    1. a "tax avoidance transaction" (or series of transactions); and
    2. has <u>at least 2 of 3 "generic hallmarks"</u>

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Background – Current Rules (cont.)

2010 Federal Budget / Enacted June 2013

- "Tax Avoidance Transaction" – any transaction (or series of transactions) that would result in a direct or indirect tax benefit, unless undertaken primarily for *bona fide* purpose other than to obtain the tax benefit

- Does not include acquisition of registered "tax shelter" investment or "flow-through shares"

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Reportable Transactions – Hallmarks

Reportable Transactions – at least 2 of 3 "Generic Hallmarks"

1. **Promoter/Advisor <u>entitled to fee</u> that is:**

   a. Based on the amount of the tax benefit from the transaction;

   b. Contingent upon obtaining tax benefit from the transaction; or

   c. Attributable to the number of persons participating in the transaction or provided access to advice from promoter/advisor about the tax consequences of the transaction

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Reportable Transactions – Hallmarks

2. **Promoter/Advisor obtains "confidential protection"**

    a. Anything that prohibits the disclosure of details or structure to another party or to the Minister of Finance

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Reportable Transactions – Hallmarks

3. Taxpayer/Promoter/Advisor has "contractual protection"

a. Any form of insurance/protection (other than standard prof liab ins)
b. Protects person against failure of transaction to achieve tax benefit
c. Pays for/reimburses any exp/fee/tax/penalty in course of tax dispute

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Reportable Transactions – Current Rules

- Who Must File & What Form?
  - Form RC312 – Information Return
  - Particular taxpayer who enjoyed the "tax benefit"
  - Any person who entered into the avoidance transaction, or series of txns, for the benefit of such particular taxpayer
  - "Promoters" and "Advisors" participating in transaction
- Deadline to File?
  - June 30th following the calendar year transaction entered
- Failure to File?
  - Penalties and denial of the expected tax benefit

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Budget 2021 Proposals

What's New?

- BEPS Action 12 Report suggested Canada's reportable transaction regime resulted in only limited reporting and did not provide for timely notification

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Budget 2021 Proposals

Budget 2021 seeks to address shortcomings with series of (proposed) amendments:

1. Changes to reportable transaction rules;
2. New requirement to report “notifiable transactions”
3. New requirement for specified large corps – report “uncertain tax treatments” (“UTT”)
4. Possible extension of normal reassessment period and introduction of penalties

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Proposed Reportable Transaction Rule Amendments – 2021

- Proposal #1 – Lower threshold for a particular transaction to be a reportable transaction (“RT”)
  - i.e. require only 1 of 3 hallmarks, instead of at least 2

- Proposal #2 – Revise “avoidance transaction” definition to include if it can be reasonably concluded that one of the main purposes of entering transaction is to obtain a tax benefit

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Proposed Reportable Transaction Rule Amendments – 2021 (cont.)

- Proposal #3 – Accelerate reporting required by taxpayer to report transaction with CRA within 45 days contract/transaction date (vs. 6 months after YE)
  - Including reporting by a promoter/advisor

- Proposal #4 – Provide for an exception to reporting requirement for advisors to the extent that solicitor-client privilege applies

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Proposed "Notifiable Transaction" Rules

- Budget 2021 proposes to introduce new category of "notifiable transactions"
  - CRA would have authority to designate w/ Dept of Finance

- Includes both transactions that CRA has found to be:
  - (i) abusive; and
  - (ii) "transactions of interest" (potential for tax avoidance or evasion but CRA requires further info)

- Requires reporting w/ CRA within 45 days of transaction
- Similar measures enacted in U.S./UK/Australia/EU/Quebec

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Proposed "Uncertain Tax Treatment" Rules

- Budget 2021 proposes to require "specified" large corporate taxpayers to report particular uncertain tax treatments ("UTT") – due w/ income tax return

- Conditions required:
  1. Cdn tax filer (Cdn corp or non-res corp with PE)
  2. Owns at least C$50 million in assets (F/S carrying value)
  3. Requires audited F/S prepared in accordance w/ IFRS (or specific GAAP relevant for pubco)
  4. Tax uncertainty reflected in audited F/S (i.e. IFRIC 23/IAS 12 - entity concluded not probable tax authority will accept UTT)

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Proposed "Uncertain Tax Treatment" Rules (cont.)

- Penalty for failure to disclose UTT
  - C$2,000 per week
  - Up to maximum of C$100,000

- UTT prescribed reporting:
  1. Amount of taxes at issue
  2. Concise description of relevant facts
  3. Tax treatment taken
  4. Whether tax uncertainty relates to a permanent or temporary tax difference

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Proposed "Uncertain Tax Treatment" Rules (cont.)

- New proposed rules would overrule FCA – *BP Canada Energy Company v. CNR, 2017 FCA 61*
  - Tax accrual working papers are not "compellable 'without restriction'"
  - Court's decision supports that automatic, ongoing access to tax accrual working papers (including UTT's) amounts to unfair requirement for taxpayer to "self-audit"
  - Under proposed rules, such requirement would be introduced based on accounting standards

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Stay Tuned…

- Consultations process included an invitation from stakeholders to provide their comments to Dept of Finance by September 3, 2021.

- Amendments made as a result of the Consultation would apply to taxation years that begin after 2021.

- Amendments would apply to transactions entered into on or after January 1, 2022.

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Q & A Session

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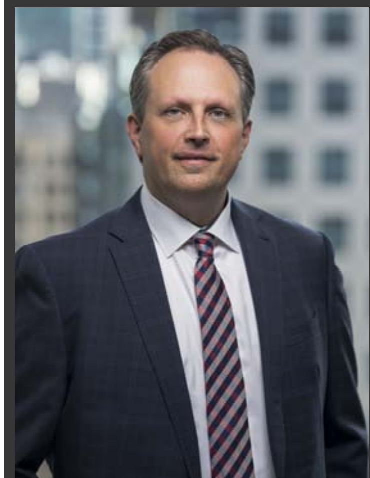
THANK YOU FOR JOINING!

YOUR SPEAKERS:



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